TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1939

No. 559

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

JULIAN PRICE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS

PETITION FOR CERTIORARI FILED NOVEMBER 28, 1939
CERTIORARI GRANTED JANUARY 15, 1940

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1939

No. 559

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

JULIAN PRICE

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

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Before United States Board of Tax Appeals

Docket No. 80540

JULIAN PRICE, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances: For Taxpayer: Julius C. Smith, Esq., D. H. Blair, Esq., J. G. Korner, Jr., Esq., Geo. D. Brabson, Esq. For Comm'r: C. P. Reilly, Esq.

Docket entries

1935

June 18—Petition received and filed. Taxpayer notified. (Fee paid.)
June 18—Copy of petition served on General Counsel.
July 12—Answer filed by General Counsel.
July 17—Copy of answer served on taxpayer.
July 30—Revised notice, copy of answer served on taxpayer.

1937

Sept. 2—Hearing set Nov. 9, 1937.
Sept. 15—Hearing set Nov. 9, 1937, Revised notice.
Oct. 1—Motion for 60 days continuance filed by taxpayer. 10/5/37 granted, continued to 2/1/38.
Dec. 22—Application for order to take depositions of Julian Price, et al., filed by taxpayer.
Dec. 22—Notice of the appearance of Geo. D. Brabson, as counsel filed.
Dec. 23—Order to take depositions of Julian Price, et al., entered.

1938

Jan. 20—Depositions of Julian Price and Rosser L. Clark filed. Taxpayer served by notary, Commissioner by Board.
Jan. 20—Copy of deposition served on General Counsel.
Feb. 1—Hearing had before Mr. Van Fossan on merits. Submitted. On motion of petitioner and respondent, depositions in toto and exhibits received in evidence. Petitioner's brief due in 30 days. Respondent's brief in 10 days, reply in 10 days.
Feb. 8—Transcript of hearing Feb. 1, 1936, filed.
Mar. 2—Brief filed by taxpayer. 2/3/28 copy served on General Counsel.
Mar. 11—Reply brief filed by General Counsel.

1938

Apr. 12—Motion for leave to file the attached reply brief, reply brief lodged, filed by taxpayer. 4/13/38 granted.

Apr. 13—Copy of motion and reply brief served on General Counsel.

Aug. 23—Memorandum findings of fact and opinion rendered, Ernest H. Van Fossan, Div. 9. Decision will be entered under Rule 50.

Sept. 7—Computation of deficiency filed by General Counsel.

Sept. 9—Hearing set Sept. 28, 1938, on settlement.

Sept. 23—Motion for a continuance to Oct. 26, 1938, filed by taxpayer 9/24/38 granted to 11/9/38.

Nov. 9—Hearing had before Mr. Arundell on settlement under Rule 50. Respondent's recomputation not contested. Referred to Mr. Van Fossan for decision.

Nov. 10—Decision entered. C. R. Arundell, Div. 7.

1939

Feb. 6—Petition for review by United States Circuit Court of Appeals, Fourth Circuit, with assignments of error filed by taxpayer.

Feb. 6—Proof of service filed by taxpayer.

Apr. 6—Agreed praecipe for record filed, with proof of service thereon.

Apr. 7—Designation of points to be urged filed by taxpayer, with proof of service thereon.

Apr. 7—Order extending time to May 1, 1939, for transmission and delivery of record, entered.

3 Before United States Board of Tax Appeals

Petition

Filed June 18, 1935

The above-named petitioner hereby petitions for a determination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (IT:AR:C-2:GL-90D) dated April 2, 1935, and as a basis of his proceeding alleges as follows:

1. The petitioner is an individual residing at Greensboro, North Carolina.

2. The notice of deficiency (a copy of which is attached and marked "Exhibit A") was mailed to the petitioner on April 2, 1935.

3. The taxes in controversy are income taxes for the calendar year 1932, in the amount of $28,946.03.

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(a) The Commissioner erroneously disallowed a loss sustained by the petitioner in the amount of $125,000;

(b) The Commissioner erroneously added to petitioner's income $4,160.00 alleged to represent a profit realized by petitioner on the sale of 26 shares of stock of Jefferson Standard Life Insurance Company; whereas the said shares were not the property of petitioner and were sold by him merely as the nominee of another and the profit thereon was erroneously included in petitioner's income.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a) In the month of September 1929, there was a merger of three banks in Greensboro, North Carolina, viz: North Carolina Bank & Trust Company, Atlantic Bank & Trust Company, and American Exchange Bank. This merger was effected in order to save the last two named banks, both of which were in a precarious financial condition. Upon an analysis being made of the assets of the Atlantic Bank & Trust Company and the American Exchange Bank, which were to be turned into the merged institution, such assets were appraised and divided into two classes which were denominated "Class A Assets" and "Class B Assets." The face value of the said "Class A Assets" was $8,723,772.74, and that of the said "Class B Assets" was $1,453,055.60. Before the newly merged institution (North Carolina Bank & Trust Company) was allowed to open for business it was required to furnish a solvent guarantee as to the value of the "Class B Assets" up to the amount of $500,000.00. The president of the Atlantic Bank & Trust Company (one of the merged banks) called upon the petitioner and two others to join him in such a guarantee.

(b) The petitioner was not a stockholder in the said bank but the financial and banking situation in Greensboro was critical and a panic seemed imminent which, if it should eventuate, would cause a financial debacle in the community and probably result in the failure of the said Atlantic Bank & Trust Company and the American Exchange Bank. Desiring to assist in averting such a debacle with its resulting losses to the community and to himself, the petitioner agreed to execute the said guaranty above referred to.

(c) Accordingly, on September 27, 1929, the petitioner, jointly with three others, executed a contract and agreement of guaranty by the terms of which they jointly and severally guaranteed the value of the said "Class B Assets" (above referred to) to the

extent of $500,000.00. The petitioner and his comakers of the said guarantee believed that the said "Class B Assets" had a value greatly in excess of $500,000 and that no liability would eventually be cast upon them by reason of their said guaranty contract.

(d) Thereupon the merged institution opened for business and listed and carried among its assets the said "Class A Assets" and "Class B Assets," and the said contract of petitioner and three others guaranteeing the said "Class B Assets" to the extent of $500,000.00. Between September 27, 1929, and September 25, 1930, the receivables, consisting of secured notes and bonds, and constituting the "Class A Assets," were reduced by collection from $8,723,772.74 to $3,155,194.57, and by August 1931, they had been further reduced by collection to $2,025,138.57; that is to say, between September 27, 1929, and August 1931, the "Class A Assets" had yielded a realization of their face value (of September 27, 1929) of $6,698,633.67. At the last mentioned date the Merger Committee valued the then remaining "Class B Assets" at $529,947.44.

(e) In June 1931, the bank called upon petitioner, and his comakers on the guaranty contract, to change the form of their guaranty so that it would be in more "bankable form," by executing their respective four notes in the amount of $125,000 each. This was done in June 1931, and the notes of the said guarantors (including petitioner) were executed and delivered in lieu of the joint and several contract of guaranty.

(f) In January 1932 there occurred a serious "run" on the merged institution, North Carolina Bank & Trust Company, which precipitated a crisis in the affairs of that bank and it was apparent that the bank would fail (it did fail later on). On April 1, 1932, the situation of the bank had grown desperate and it was ascertained that due to the depression and panic conditions obtaining in the country, the "Class B Assets" had shrunk to a point where there was no remaining value in them and that the full liability upon petitioner's guaranty was established. Thereupon demand was made upon petitioner for the payment of his note of $125,000.

(g) Petitioner did not have available the cash with which to discharge his said note but arranged with the bank to accept property in the form of high-grade securities which he then turned over to the bank, in the amount of $125,000.00.

(h) The bank was insolvent and on the verge of failure (it did fail thereafter) and investigation disclosed that there was no possibility of petitioner recovering assets out of which to recoup himself for the loss then sustained by him.

(i) Petitioner, pursuant to his written obligation of guaranty, parted with his property in the amount of $125,000.00, and thereby sustained a deductible loss in the year 1932, in the amount of $125,000.00.

(j) Petitioner took deduction for his said loss in his tax return for 1932; the Commissioner has disallowed the loss and restored $125,000.00 to taxable income of petitioner.

(k) On or about November 22, 1932, petitioner was indebted to his son, R. C. Price, for moneys which he had borrowed from him. In that year petitioner found an opportunity to buy 26 shares of the capital stock of Jefferson Standard Life Insurance Company at an advantageous price of $4,940 and accordingly purchased them at the said price for and on the account of the said R. C. Price. The certificates were issued in the name of R. C. Price and were delivered to R. C. Price by the petitioner. Shortly thereafter petitioner was called upon to raise a considerable sum of money, and, in order to raise the said funds, the petitioner sold a considerable amount of securities held by him and, in addition thereto, borrowed other and similar securities from others. Among such, the petitioner borrowed a considerable number of shares of Jefferson Standard Life Insurance Company stock from his son, R. C. Price, and among such borrowed shares were the said 26 shares of Jefferson Standard Life Insurance Company stock, which were referred to above. Petitioner thereupon
8 sold the securities which he had borrowed from his son and others, along with those owned by himself, in order to raise the funds above referred to. Among such securities sold by petitioner, as aforesaid, were the shares borrowed from R. C. Price, among which were the said 26 shares of Jefferson Standard Life Insurance Company stock. In order to transfer a proper title the petitioner caused the said 26 shares to be transferred into his name. Petitioner sold all of the said shares, including the said 26 shares. On all of such stock sold at an advance in price, the profit was duly reported by the owner thereof, i. e., the lender of the stock to petitioner. Likewise, R. C. Price reported in his tax return as his profit the gain realized on the sale by petitioner of the stock borrowed from him (R. C. Price). The small block consisting of the said 26 shares were sold for $9,100.00 and the gain thereon was $4,160, which R. C. Price reported as his taxable profit. The Commissioner has added to petitioner's income the said amount of $4,160, alleging the said amount to represent a profit to the petitioner. This the petitioner denies.

Wherefore, the petitioner prays the Board to hear this proceeding and to decide and order (1) that petitioner sustained a deductible loss of $125,000.00 in the year 1932, and (2) that the

profit of $4,160.00 on the sale of 26 shares of Jefferson Standard Life Insurance Company stock was not the profit of
9 petitioner and did not constitute taxable income to the petitioner.

(S) JULIUS C. SMITH,
Julius C. Smith,
(S) D. H. BLAIR,
D. H. Blair,
(S) J. G. KORNER, Jr.,
J. G. Korner, Jr.
Transportation Bldg., Washington, D. C.,
Attorneys for petitioner.

[*Duly sworn to by Julian Price; jurat omitted in printing.*]

10 *Exhibit A to Petition*

SN–A.

IT:AR:C–2.
GL–90D.

APR. 2, 1935.

Mr. JULIAN PRICE, *Greensboro, North Carolina.*

SIR: You are advised that the determination of your income tax liability for the year(s) 1932, discloses a deficiency of $28,946.03, as shown in the statement attached.

In accordance with section 272 (a) of the Revenue Act of 1932, as amended by section 501 of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P–7. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,
Commissioner.
By (Signed) CHAS. T. RUSSELL,
Deputy Commissioner.

Enclosures:
Statement.
Form 870.
GL/EW–1.

11 STATEMENT

IT:AR:C-2.
GL-90D.

In re: Mr. Julian Price, Greensboro, North Carolina

Income Tax Liability

Year, 1932: Income Tax Liability, $30,365.67; Income Tax Assessed, $1,419.64; Deficiency, $28,946.03.

The deficiency shown herein is based upon the reports dated February 6, 1934, and May 2, 1934, prepared by Revenue Agent C. F. Strandberg and transmitted to you under dates of February 20, 1934, and May 9, 1934. In Bureau letter dated September 27, 1934, you were advised that the agent's reports referred to above had been approved by this office. Your protest relative thereto has been carefully considered in connection with the information presented at a conference in this office with your representative October 24, 1934.

Net income reported in return	$23,220.47
Add:	
1. Interest paid	3,750.00
2. Losses	125,000.00
3. Profit on sales	23,225.00
Net income adjusted	$175,195.47

Explanation of Changes

1. Interest deduction has been reduced from $31,958.24 to $28,208.24 due to the elimination of two items of $1,875.00 which were not actually paid in cash in the year 1932.

2. The deduction claimed by you which has been disallowed represents your share of the guarantee, in the merger of the Atlantic Bank and Trust Co. with the North Carolina Bank and Trust Co. that class A assets taken over by the new bank should be made good.

The guaranty contract was executed by you and three other individuals, each one being jointly and severally liable to the extent of $500,000.00.

The North Carolina Bank and Trust Co. took over the class A assets of the old bank in 1929, the class B assets being pledged to make the class A assets good. In the year 1931 it became apparent that the class B assets were not sufficient to cover the losses and the guarantors were each called upon to make the payments under their contract.

12 You as one of the guarantors executed in the year 1931 a note for $125,000.00, and also endorsed the note of another guarantor, Mr. C. W. Gold, in the amount of $125,000.00. Mr. Gold's note was secured by a $50,000.00 life insurance policy which, as it later developed, was allowed to lapse, and stock of the Jefferson Standard Life Insurance Co. standing in the name of your wife. As collateral for your own note you also borrowed from your wife.

In April 1932 you gave your note for $50,000.00 covering your original $125,000.00 note and the $125,000.00 note of Mr. Gold. This was fully secured by collateral. At the maturity of the note in 1933 the bank accepted in payment bonds of an equal amount of the Southwestern Realty Co. and the bank endorsed the note over to your wife and daughter.

In your 1932 return you claimed as a deduction $125,000.00 representing your pro rata share of the guaranty, which you considered a loss at that time. This is not the year in which the note was paid.

You contend that you did not claim the deduction in the year 1931 for the reason that you did not believe that a loss on the note would eventually be sustained; that in 1932 you first placed property of your own with the bank as collateral, at which time you substituted securities of your own for those borrowed from members of your family, and that as a result the note when finally paid in 1933 was endorsed over to the members of your family from whom you had previously borrowed the securities; which under the circumstances was equivalent to paying the debt in 1932 when you first put up collateral of your own. On the basis of the evidence the loss should be allowed either in the year 1931 when you first gave your note and when the other guarantor who was able to pay, paid his note in cash or in the year 1933 when the indebtedness was settled and the note surrendered.

Your income is reported on the cash receipts and disbursements basis, and under several decisions of the courts and the United States Board of Tax Appeals a taxpayer on the cash receipts basis who is an endorser or guarantor of notes of another when called upon to make good his endorsement by giving his personal note therefor does not suffer a deductible loss until the obligation is finally paid. (Eckert v. Burnet, 383 U. S. 140, James K. Bowen, 27 Board of Tax Appeals Reports, page 824; and Edward A. Hughes, 27 Board of Tax Appeals Reports, page 1022).

It is held by this office that under the provisions of section 23 (j) of the Revenue Act of 1932 the loss is not one sustained in the year 1932.

3. The profit on sale of stock in the Jefferson Standard Life Insurance Co. has been increased from $129,240.00 to $152,465.00, determined as follows:

Computation of Cost of 800 Shares of Jefferson Standard Life Insurance Co. Sold in 1932

C. Stock Held More Than Two Years

Acquired from	Date acquired	Shares sold	Sale price	Cost	Profit
C. C. Taylor	11-15-19	100		$15,000.00	
Julian Price, Trustee	2-11-13	100		6,750.00	
Julian Price, Trustee	2-11-13	100		6,750.00	
C. C. Taylor	11-15-19	100		15,000.00	
I. H. Gantt	3-22-26	5		1,500.00	
T. C. Smith	3-22-26	20		6,500.00	
P. B. Falls	8-25-26	1		400.00	
A. G. Meyers	8-25-26	3		1,200.00	
Atlantic Bank, Trustee	8-25-26	1		100.00	
Total		430	$150,500.00	$53,000.00	$97,500.00

Stock Held Less Than Two Years

G. A. and Mrs. Holderness	10-20-32	100		$21,000.00	
R. C. Price	12-5-32	50		17,500.00	
B. C. Mayo	12-5-32	50		17,500.00	
R. C. Price	12-5-32	20		7,000.00	
R. C. Lucas	8-2-32	10		1,170.00	
J. E. Vochringer, Jr.	8-2-32	15		2,265.00	
R. C. Price	12-5-32	80		14,240.00	
Mrs. C. W. Gold	10-20-32	97		9,120.00	
G. A. Holderness	10-20-32	3		600.00	
S. Hallhonor	12-5-32	1		530.00	
Albert Anderson	12-5-32	1		800.00	
Totals		350	$129,500.00	$74,535.00	$54,965.00
Total					$152,465.00

It will be noted that $97,500.00 of the profit is considered capital net gain and $54,965.00 ordinary gain.

You have protested the inclusion of $4,100.00 profit on sale of 26 shares which were acquired December 5, 1932, from your son, R. C. Price, on the grounds that the sale was one made by your son.

The records, however, of the North Carolina Bank and Trust Co. show that a check was issued by you November 22, 1932, in the amount of $4,940.00, and that the proceeds of the sale were received by you. There is no indication that the profit on the sale was turned over to your son. The profit on the sale is one held to have been realized by you.

14 **Computation of Tax**

Net income		$175,195.47
Less: Capital net gain		97,500.00
Net income subject to surtax		$77,695.47
Less:		
Dividends	$8,248.00	
Personal exemption	4,100.00	
		12,348.00
Balance subject to normal tax		$65,347.47
Normal tax at 4% on $4,000.00		160.00
Normal tax at 8% on $61,347.47		4,907.80
Surtax on $77,695.47		13,110.27
Capital net gain at 12½% on $97,500.00		12,187.50
Total tax assessable		$30,365.67
Previous assessment		1,419.64
Deficiency		$28,946.03

15 **Before United States Board of Tax Appeals**

[Title omitted.]

[File endorsement omitted.]

Answer

Filed July 12, 1935

The Commissioner of Internal Revenue, by his attorney, Robert H. Jackson, Assistant General Counsel for the Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

1. Admits the allegations of paragraph 1.

2. Admits the allegations of paragraph 2.

3. Admits the taxes in controversy are income taxes for the calendar year 1932, but denies that the amount is $28,946.03.

4. (a) Denies the error complained of in paragraph 4 (a).

(b) Denies the error complained of in paragraph 4 (b).

5. (a) Admits the matter set forth in the first, second, third, fifth, and sixth sentences of paragraph 5 (a), and denies the remainder thereof.

(b) Admits the petitioner agreed to execute the said guaranty above referred to, and denies the remainder of paragraph 5 (b).

(c) Admits that accordingly, on September 27, 1929, the petitioner, jointly with three others, executed a contract and agreement of guaranty, and denies the remainder of paragraph 5 (c).

(d) Admits that thereupon the merged institution opened for business and listed and carried among its assets the

16 said "Class A Assets" and "Class B Assets," and the said

contract of petitioner and three others, and denies the remainder of paragraph 5 (d).

5. (e) Admits that in 1931, the petitioner, and his co-makers, on the guaranty contract, executed their respective four notes in the amount of $125,000 each, and denies the remainder of paragraph 5 (e).

(f) Denies the matter set forth in paragraph 5 (f).

(g) Denies the matter set forth in paragraph 5 (g).

(h) Denies the matter set forth in paragraph 5 (h).

(i) Denies the matter set forth in paragraph 5 (i).

(j) Admits that petitioner took deduction for an alleged loss of $125,000.00 in his tax return for 1932; that the Commissioner disallowed it and restored $125,000.00 to taxable income of petitioner, and denies the remainder of paragraph 5 (j).

(k) Admits that during the year 1932, petitioner sold a considerable amount of securities held by him, and denies the remainder of paragraph 5 (k).

Denies, generally and specifically, each and every allegation in the taxpayer's petition contained not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the taxpayer's appeal be denied.

(Signed) ROBERT H. JACKSON,
Assistant General Counsel
for the Bureau of Internal Revenue.

Of Counsel:
J. E. MARSHALL,
PAUL E. WARING,
Special Attorneys,
Bureau of Internal Revenue.

JEM/cal 7/11/35.

17 Before United States Board of Tax Appeals

JULIAN PRICE, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket No. 80540

Where petitioner, in order to put his obligation as a guarantor in more bankable form, gave a bank his personal note, which note he subsequently "paid" by the giving of another note for the amount of his original note and the note of another, Held, petitioner may not deduct as a loss the amount of his original

note, no actual payment for the new note having been made in the taxable year.

David H. Blair, Esq., and George D. Brabson, Esq., for the petitioner.

Charles P. Reilly, Esq., for the respondent.

Memorandum findings of fact and opinion

Aug. 23, 1938

This proceeding was brought for a redetermination of a deficiency of $28,946.03 in petitioner's income tax for the calendar year 1932.

Two questions are presented by the case. The first concerns the deductibility as a loss under section 23 (e) of the Revenue Act of 1932, of an alleged payment whereby petitioner satisfied his obligations as guarantor by giving a bank his personal note in the amount of the obligation and at the same time receiving from the bank his personal note theretofore given the bank in order that the guaranty might be "in more bankable form."

The second question is whether petitioner's income for the taxable year should be increased by an amount of profit arising out of the sale of certain stock which, upon a prior purchase by petitioner, had been given to and placed in the name of petitioner's son.

18 *Findings of fact*

The petitioner is a resident of Greensboro, North Carolina, and filed a joint return with his wife for the taxable year in question. This return was filed on a cash receipts and disbursements basis.

During the year 1929 petitioner was a stockholder of the Atlantic Bank and Trust Company of Greensboro (hereinafter called Atlantic Bank). Petitioner at that time was also president and a substantial stockholder of the Jefferson Standard Life Insurance Company of Greensboro (hereinafter called Jefferson Standard Life), which company owned 1,543 shares of stock and was a large depositor in the Atlantic Bank. As a stockholder and officer of the Jefferson Standard Life petitioner was vitally interested in its investment and deposit in the Atlantic Bank.

During the month of September 1929 the Atlantic Bank was a party to a plan for the merger of a number of banks and trust companies in the Greensboro territory. The directors of the several banks and trust companies had agreed upon a plan of

merger, and a committee had been formed to pass upon the assets tendered by the several merging banks. After making an appraisal of the assets of the Atlantic Bank the merger committee decided that it could not accept the Atlantic Bank assets as sufficient to cover the obligations of that bank to be assumed by the North Carolina Bank and Trust Company, which was to be the name of the newly formed bank (hereinafter called North Carolina Bank), unless some guaranty of those assets was given. Realizing that it would be quite detrimental to the Atlantic Bank to be eliminated from the merger after the
19 plan of merger had already been made public the four principal stockholders of the Atlantic Bank agreed to and did execute the required guaranty. The four stockholders executing this guaranty were Julius W. Cone, Charles W. Gold, J. S. Duncan, and petitioner.

For the purposes of the merger and guaranty agreement the assets of the Atlantic Bank were divided into two classes, designated "conditionally accepted," or "A" assets, and "pledged assets" or "B" assets. Pursuant to the guaranty agreement the "B" assets were delivered to the newly formed North Carolina Bank, in trust, with authority to charge any losses which might be established in the "A" assets, within a specified time, against the account of the "B" assets. The guaranty was fixed under the merger agreement at two years from September 28, 1929, but was subsequently extended by consent of the guarantors to September 28, 1932.

The above-mentioned guaranty was dated September 27, 1929, and provided in substance that if the North Carolina Bank failed to realize a certain sum from the "A" assets within two years from September 28, 1929, the four guarantors jointly and severally would make up the deficiency so ascertained in an amount not exceeding $500,000; that the "B" assets were to be used to apply first to any losses occurring in the "A" assets, and any balance then remaining in the "B" assets was to be used to reimburse the four guarantors for any sums that may have been paid under the guaranty.

The North Carolina Bank commenced business with the assets of the several merged banks and continued to operate as a general banking institution for several years. The bank ad-
20 ministered the above-mentioned "B" assets in accordance with the provisions of the merger and guaranty agreement.

In June 1931 the president of the North Carolina Bank advised the guarantors that the "B" assets were not in such shape that the bank could use them to the extent necessary for bankable purposes and, therefore, the bank requested the guarantors to put

their guaranty into bankable form so that it could be used to obtain bank credit. In compliance with this request petitioner executed and delivered to the bank his note for $125,000 and endorsed a similar note of C. W. Gold for the same amount. In consideration for the execution of these notes on the part of petitioner the bank agreed that the liability of petitioner under the guaranty should not be in excess of $250,000.

Security was placed with the bank for petitioner's note by the deposit as collateral of 4,000 shares of Pilot Life Insurance Company stock standing in the name of petitioner's wife. On November 14, 1931, these 4,000 shares were exchanged for 400 shares of Jefferson Standard Life stock belonging to petitioner's wife. There was also deposited as collateral a life-insurance policy on petitioner's life in the face amount of $100,000, payable to petitioner's wife as beneficiary.

Collateral for the Gold note was 400 shares of Jefferson Standard Life stock standing in the name of petitioner's wife and an insurance policy in the face amount of $50,000 on the life of Gold.

On December 23, 1931, 200 shares of the Jefferson Standard Life stock which had been deposited as collateral on the Price note were released and in lieu thereof there was deposited as collateral 50 shares of Jefferson Standard Life stock belonging to petitioner's wife and 500 shares of Greensboro News Company's preferred stock belonging to petitioner's daughter.

Thus on December 23, 1931, there was the following collateral for both notes: 650 shares of Jefferson Standard Life stock belonging to petitioner's wife, 500 shares of Greensboro News Company stock belonging to petitioner's daughter, and the above-mentioned insurance policies.

All of this security was still held by the bank on March 28, 1932, the time of the transaction here in issue, and was retained as collateral for petitioner's note of that date for $250,000.

In August 1931 the North Carolina Bank had an appraisal made as of that date of all its assets, including the "B" assets held by it as trustee. This appraisal was made on the basis of the fair market value of the assets at that time and showed a total value remaining in the "B" assets of $529,947.44.

At the end of 1931 the guaranty agreement was still in force and effect. The "B" assets were still in the hands of the North Carolina Bank, as trustee, and were still in the process of collection. No demand had ever been made upon petitioner for the payment of any part of his obligation under the guaranty. While it was known that there would be some loss to the guarantors it was not definitely known throughout 1931 what the

amount of the loss would be, and the guarantors had every reason to believe there would be a substantial reimbursement from the "B" assets of any losses.

It was on September 28, 1931, that the guarantors signed the above-mentioned extension of time for the final liquidation of the "B" assets to September 28, 1932.

22 Late in December 1931 a run was made on the United Bank and Trust Company of Greensboro, the only other commercial bank then in operation in the city, causing it to close its doors and fail on the same day the run occurred.

The failure of the United Bank and Trust Company precipitated a similar run on the North Carolina Bank on the same day. After the first active run on the North Carolina Bank was over, withdrawals continued throughout the best part of January 1932, and the deposits withdrawn never came back. By borrowing approximately $8,000,000 from the Reconstruction Finance Corporation the bank was able to stay open.

The closing of the United Bank and Trust Company and the run on the North Carolina Bank brought about a marked change in the value of all the bank's assets, and especially the "B" assets.

Conditions in Greensboro and the condition of the bank's assets had grown worse throughout the first part of 1932, and collections had diminished on both "A" and "B" assets to such an extent that there was no possibility of recovering anything from the "B" assets.

In the latter part of March 1932 petitioner, in his discussions with officials of the North Carolina Bank, was informed that the bank had decided that the possibilities of collecting anything on the "B" assets were remote and that there was no hope of any relief from these assets. The bank requested that petitioner make a final settlement of his obligation under the two notes and the guaranty to the bank. Petitioner proposed to pay the two notes (his own note and Gold's note on which he was endorser) by giving the bank his note for $250,000. The bank accepted,

23 and the C. W. Gold note in the amount of $125,000, endorsed by petitioner, and petitioner's individual note in the same amount were paid by the note of petitioner in the amount of $250,000, dated March 28, 1932.

Upon the delivery of this note for $250,000, the bank marked "paid" and turned over to petitioner the two notes which had been executed under the guaranty agreement. Both petitioner and the bank considered this to be a final payment of the two notes given under the guaranty. Petitioner deducted as a loss on his 1932 return the sum of $125,000, the amount of his own note theretofore held by the bank.

C. W. Gold died the latter part of 1932, and it was necessary for petitioner to look to Gold's estate for reimbursement of the $125,000 paid on account of his note. The estate, under the laws of North Carolina, had one year within which to collect the assets and settle the estate. The $50,000 insurance policy on Gold's life, which had been deposited as collateral, had been allowed to lapse. In 1933 it became apparent that petitioner could expect no reimbursement or recoupment from the Gold Estate, and the loss thereon was claimed and allowed for that year.

The bank retained the same security for the $250,000 note as it previously held under the two guaranty notes. In December 1932 petitioner requested the bank to allow him to substitute certain securities of his own for those of his wife and daughter. This request was granted, and in that month petitioner substituted 600 shares of Jefferson Standard Life stock of his own in lieu of 600 shares of stock of the same company belonging to his wife.

24 Early in 1933 petitioner purchased for his wife's account $100,000 par value North Carolina B. & T. Buildings, Inc., bonds. Shortly thereafter petitioner's daughter, Kathleen Price Bryan, acquired $150,000 additional bonds of the same company by exchange for $150,000 par value shares of stock in Greensboro News Company, with the Pilot Insurance Company. On November 18, 1933, petitioner's $250,000 note, together with all securities attached, was transferred and assigned by the bank's conservator, without recourse, to petitioner's wife and daughter in consideration of the transfer to the conservator of the $250,000 bonds of North Carolina B. & T. Buildings, Inc., which bonds had been acquired as aforesaid. Petitioner's note and the securities attached are now held by his son-in-law, Mr. Bryan, as agent or trustee for Mrs. Price and Mrs. Bryan.

In 1930 petitioner borrowed $150,000 from his son, Ralph C. Price, and on or about November 22, 1932, was still heavily indebted to him.

Petitioner had an opportunity, on or about this last mentioned date, to purchase 26 shares of Jefferson Standard Life stock at $4,940, which was an advantageous price. This stock was purchased by petitioner with his own money. It was transferred to petitioner's son's name and was delivered to and held by the son.

About the time of the above-mentioned purchase petitioner was negotiating to sell 1,000 shares of Jefferson Standard Life stock. This sale was consummated early in December of the taxable year. Included in the 1,000 shares sold were the 26 shares above-mentioned which petitioner had had transferred to himself so that he could effect the sale. The sale price for

25 the 26 shares in question was $9,100, or a gain of $4,160. After the sale petitioner gave his son no money but states that he will give him credit for the gain when the final settlement is made of petitioner's indebtedness to his son. It had not been made by January 1938. Petitioner's son, and not petitioner, reported the $4,160 on his 1932 Federal income tax return as gain.

Opinion

VAN FOSSAN: We first address ourselves to the question of the deductibility of the alleged payment in March 1932 in settlement of petitioner's liability under the guaranty agreement.

Respondent bottoms his entire argument on this issue on Eckert v. Burnet, 283 U. S. 140, and Frank Kuhn, 34 B. T. A. 274, together with the facts that petitioner was on a cash receipts and disbursements basis and paid the bank no cash in the taxable year in question.

The Eckert case is authority for the rule that a taxpayer on the cash basis may not, until he pays the note, deduct, either as a sustained loss or as a bad debt, the amount of a note made by him as primary obligor in substitution for a note given by another upon which the taxpayer had theretofore been a secondary obligor.

In Frank Kuhn, supra, the taxpayer, recognizing the rule of the Eckert case, sought to distinguish it on the basis that he had made a pledge of property to collaterally secure the new note. This argument was rejected, it being said that it

"* * * treats the pledge as if it were a loss of the property. This clearly is not correct. Title to the property continues in the pledgor, and by paying the debt he may retake possession. * * * Thus the loss is no more realized in this case because the taxpayer has deposited collateral than in the Eckert case, where collateral was not mentioned."

26 Petitioner in the present case, conceding the rule of the Eckert case, seeks to show that the rule is not applicable with reference to his personal liability on the guaranty upon the facts.

His theory of the case, in substance, is that his liability under the guaranty agreement and the note given to put the guaranty in more bankable form, was a contingent liability and did not become fixed and determined until March 1932, when the bank informed him that the "B" assets were not going to be sufficient to meet the failures or deficiencies in the "A" assets and that it was not until then that he agreed to pay this liability by giving the bank his note for $250,000, collaterally secured, and the bank agreed to accept this note as payment. On this premise he argues

that he was not giving one note in lieu of another, but was paying a new obligation that was not fixed until that time.

Petitioner seeks to prove his case by citation of authorities to the effect that payment is whatever the parties to the transaction consider payment. As an abstract rule of law this might be conceded; but it misses the gist of the conception of "payment" under the income tax laws when the taxpayer is on the cash basis. Payment for this purpose contemplates an outlay of cash, or its equivalent, and not a mere shifting of the nature of the liability. In such a situation a loss may become fixed and determined at a particular time, but it is not sustained until paid. The payment contemplated is an actual payment of cash. As was said in Hart v. Commissioner, 54 Fed. (2d) 848, and quoted in Jacob F. Schoellkopf, Jr., 35 B. T. A. 855:

27 "It is inconsistent with the cash receipts and disbursements method of accounting that the petitioner be permitted to claim a deduction where there has been no actual payment of cash. This basis of accounting requires that he report only actual receipts and deduct only actual disbursements."

A. W. D. Weis, 13 B. T. A. 1284, is relied on by petitioner. However, as was said in Frank Kuhn, supra, the distinction between the Weis case and Eckert v. Burnet, supra, "appears in Burn Manufacturing Co. v. Commissioner, 59 Fed. (2d) 504, in which it is also said that the Weis case must be regarded as overruled by the Eckert case, in so far as it considers the cash basis." See Max Gross, 36 B. T. A. 759.

Petitioner calls attention to certain language in John C. Hermann, 27 B. T. A. 409, which he urges is still a fair statement of the law notwithstanding S. E. Thomason, 33 B. T. A. 576. This language is, in line with the principle enunciated many times,[1] that an obligation of a taxpayer on the cash basis may be deducted when paid with borrowed funds for which taxpayer has given his note and posted collateral. That, however, is not the present situation.

In our opinion petitioner's case is clearly within the rule as laid down by the Supreme Court in the Eckert case and followed or recognized in subsequent cases.[2] Although petitioner's

28 liability prior to March 1932 arose out of the guaranty agreement and the note was given to put that guaranty

[1] Crain v. Com'r, 75 Fed. (2d) 962; Menihan v. Com'r, 79 Fed. (2d) 304; and Humphrey v. Comm., 91 Fed. (2d) 155; Robert B. Keenan, 20 B. T. A. 498.

[2] Page v. Rhode Island Hospital Trust Co., 80 F. (2d) 192, aff'g Rhode Island Hospital Trust Co. v. Page, 14 F. Supp. 481; Menihan v. Com'r, 79 F. (2d) 305; Crain v. Com'r, 75 F. (2d) 962; Max Gross, 36 B. T. A. 759; Jacob F. Schoellkopf, Jr., 35 B. T. A. 855; Edmund A. Hughes, et al., 27 B. T. A. 1022; E. C. Pratt, 23 B. T. A. 148; Herman Axelrod, 18 B. T. A. 927; T. Harvey Ferris, 38 B. T. A. — (Aug. 11, 1938); cf. Ben Greenbaum, 20 B. T. A. 469.

into bankable form, it cannot be said that petitioner had no liability on the agreement and on the note. If this were true the execution of the agreement, the giving of the note, and the depositing of collateral therefor would have been empty gestures. Petitioner's personal liability was contingent, but in our opinion is comparable to the liability of an endorser, which was the situation in Eckert v. Burnet, supra. For present purposes there is no distinction. Petitioner has satisfied his liability as guarantor under the guaranty agreement and note by a shifting of the form of his liability. His liability under the guaranty agreement and note could have been met by a sale or forfeit of the collateral, but rather than have this take place petitioner elected to give a new note promising to pay in the future.

Whether or not petitioner suffered an economic diminution of his estate may be grounds for abstract argument, but it is clear that he made no outlay of cash in the purported payment. As we have before stated, this is the real guide for determining whether petitioner suffered a loss in the taxable year in question. Petitioner's loss is deductible in the year in which he pays the note.

We believe that the second question of this case, concerning the taxability of a profit on the sale of certain stocks, must be decided in favor of petitioner, who claims that in the sale of the stocks in question he was acting on behalf of his son. Even after subjecting this entire transaction to the close scrutiny prescribed for intra-family dealings (John E. Zimmerman, 29 36 B. T. A. 279; Nathan R. Adlen, 38 B. T. A. — (July 22, 1938)), no lack of bona fides is evident.

Petitioner had a business reason for having the stock, upon its purchase by him, transferred in his son's name and physically delivering the stock to his son. He was liquidating in part a long-standing indebtedness to his son. When the stock was thereafter transferred to petitioner's name and delivered to him it was for the purpose of facilitating the sale of the large block of the same stock being sold by petitioner. The 26 shares of stock being sold were none the less the property of petitioner's son. The further fact that petitioner's son reported the gain thereon in his 1932 Federal income-tax return is persuasive of the status of the stock's ownership.

For respondent to prevail on this issue it would be necessary to discredit completely petitioner's testimony. We can find no justification in the record for such action.

Decision will be entered under rule 50.

Entered August 23, 1938.

Enter:

30 Before United States Board of Tax Appeals

Docket No. 80540

JULIAN PRICE, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Pursuant to memorandum opinion entered August 23, 1938, the respondent in the above entitled proceeding filed a proposed computation with the Board on September 7, 1938, and the case having been called for settlement on November 9, 1938, at which time no objection was offered to the respondent's proposed computation, it is

Ordered and decided: That there is a deficiency in income tax for the year 1932 in the amount of $27,144.92.

(Signed) C. R. ARUNDELL,
Member.

Enter:
Entered Nov. 10, 1938.

31 In United States Circuit Court of Appeals for the Fourth Circuit

United States Board of Tax Appeals, Docket No. 80540

JULIAN PRICE, PETITIONER ON REVIEW

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, RESPONDENT ON REVIEW

Petition for review and assignments of error

Filed Feb. 6, 1939

To the Honorable Judges of the United States Circuit Court of Appeals for the Fourth Circuit:

Now comes Julian Price in support of this, his petition for review, filed pursuant to the provisions of section 1001 of the Revenue Act of 1926, as amended by section 1001 of the Revenue Act of 1932, for review of the decision of the United States Board of Tax Appeals entered November 10, 1938, determining

and ordering a deficiency in income tax against this petitioner for the calendar year 1932, in the amount of $27,144.92, and respectfully shows:

I

Your petitioner on review hereinafter referred to as the taxpayer is an individual residing at Greensboro, North Carolina, and filed his income-tax return for the year 1932 with the Collector of Internal Revenue for the District of North Carolina, whose office is located in the city of Raleigh, North Carolina.

Your respondent on review hereinafter referred to as the Commissioner is the duly appointed, qualified, and acting Commissioner of Internal Revenue of the United States.

32 II

The Commissioner determined a deficiency in Federal income taxes against the taxpayer for the calendar year 1932 in the amount of $28,946.03, and on April 2, 1935, in accordance with the provisions of section 272 of the Revenue Act of 1932, sent to the taxpayer by registered mail a notice of said deficiency. Thereafter, on June 18, 1935, the taxpayer filed his appeal from said notice of deficiency to the United States Board of Tax Appeals, being docket No. 80540.

On August 23, 1938, the Board of Tax Appeals promulgated its memorandum opinion and on November 10, 1938, entered its final order and decision in said cause, wherein and whereby the Board decided that the deficiency determined by the Commissioner was correct, except for one minor issue which the Board decided for the taxpayer, and that there was a deficiency against the taxpayer for the year 1932 in the amount of $27,144.92.

The opinion of the Board of Tax Appeals is not reported.

III

The nature of the controversy is as follows:

Taxpayer is an individual, married and living with his wife in Greensboro, North Carolina. He and his wife filed a joint return for the year in question.

During the year 1929 taxpayer was a stockholder and director in the Atlantic Bank & Trust Co. of Greensboro, N. C. Taxpayer was also president of, as well as a large stockholder in, the Jefferson Standard Life Insurance Co. of Greensboro, which company owned 1,543 shares of the capital stock of the same bank; hence the taxpayer was vitally interested both personally
33 and as an officer in the welfare of the Atlantic Bank & Trust Co.

During September 1929 a plan was in progress for the merger of a number of banks in Greensboro and the surrounding cities. The directors of several banks had agreed upon a plan of merger, and a merger committee was formed to pass upon and accept or reject the assets tendered by the several banks, including the Atlantic Bank & Trust Co. Taxpayer, as a director of Atlantic Bank & Trust Co., attended several meetings of this merger committee. That committee made an appraisal of the assets of the several banks to determine what assets should be taken over by the new bank.

The merger committee finally decided that it would not accept the assets of Atlantic Bank & Trust Co. as sufficient to cover the obligations of that bank to be assumed by the new bank, known as North Carolina Bank & Trust Co., unless some guaranty of those assets was given. To prevent the Atlantic Bank & Trust Co. from being eliminated from the merger, taxpayer and three other stockholders of that bank, to wit, Julius W. Cone, C. W. Gold, and J. S. Duncan, agreed to and did execute the required guaranty in the amount of $500,000.

Accordingly, the assets of Atlantic Bank & Trust Co. were divided into two classes, designated "conditionally accepted" or Class A assets, and "pledged assets" or Class B assets. Under this guaranty agreement the Class B or pledged assets were delivered to the North Carolina Bank & Trust Co. in trust, to collect, and, if it became necessary, to charge any losses which might be established in the Class A assets within a two-year period, against the pledged or Class B assets. This guaranty period was subsequently extended by consent of the guarantors
34 to September 28, 1933.

The guaranty provided, in brief, that the North Carolina Bank & Trust Co. should proceed to administer and to collect both classes of assets; that if the Bank failed to realize a fixed amount from the Class A assets within two years from September 28, 1929, the four guarantors would jointly and severally make up any deficiency so ascertained, in an amount not exceeding $500,000, with the further provision, however, that the Class B assets should be used to apply first to any losses occurring in the Class A assets, and second to reimburse the guarantors for any liabilities incurred under the guaranty.

The North Carolina Bank & Trust Co. commenced business with the assets of the several merged banks, and operated as a banking institution for several years. It administered the Class B assets in accordance with the provisions of the guaranty agreement.

In June 1931 the North Carolina Bank & Trust Co. advised the four guarantors that the Class B assets were not in such

shape that the bank could use them to the best advantage for banking purposes, and accordingly requested the guarantors to put their guaranty in more bankable form in order that it could be used to obtain bank credit. Accordingly, the guarantors agreed to execute and deliver to the bank their several notes for $125,000 each. Taxpayer also agreed to endorse C. W. Gold's note, and in consideration the bank agreed that petitioner's liability under the guaranty should not exceed the $250,000 evidenced by these two notes. Taxpayer also agreed that as a further security under his guaranty he would put up certain shares of stock to secure the payment of the two notes.

35 In August 1931, the North Carolina Bank & Trust Co. had an appraisal made of all its assets, including the Class B assets which it held as trustee. This appraisal showed a fair market value of the Class B assets amounting to $529,947.44 as of August 31, 1931.

On September 28, 1931, the guarantors signed an agreement consenting to the extension of the time for collection of the Class B assets to September 28, 1932.

Up to the end of 1931 the guaranty agreement was still in full force and effect. The Class B assets were still held by the Bank and were in process of collection. No demand had ever been made upon any of the guarantors for payment of any part of their obligations under the guaranty. While it was known that there would be some liability on the part of the guarantors, it was not definitely known how much the loss would be and the guarantors had every reason to believe that there would be a substantial recovery and reimbursement from the Class B assets of any losses occurring under the guaranty.

Late in December 1931, however, a disastrous run occurred on the banks in Greensboro, closing all the other commercial banks except the North Carolina Bank & Trust Co. The failure of the other banks which followed precipitated similar runs on the North Carolina Bank & Trust Co. These runs continued throughout January 1932, and quiet withdrawals continued thereafter. After these bank failures and runs had continued for some months, financial and business conditions in Greensboro and the surrounding territory became distressing, and were so

36 demoralized that the people were in desperate straits for credit or funds. Securities dropped precipitously in value. These circumstances brought about a changed condition in the value of banking assets which seriously affected the whole financial structure and eventually caused the Bank to fail. The Class B assets were badly affected as they were the lowest down in the scale.

Conditions grew worse throughout the early part of 1932, and during the first few months of that year collections on both Class A and Class B assets decreased to such a point that it became evident there was no possibility of realizing anything from the Class B assets. Taxpayer, as a member of the Executive Committee of the North Carolina Bank & Trust Co. discussed these conditions with officials of the Bank, as well as the matter of his guaranty.

In the latter part of March 1932, taxpayer was finally informed by the Bank officials that the possibility of collecting anything on the Class B assets had decreased to such a point that there was no longer any hope of relief from that source. The Bank, therefore, requested taxpayer to make a final settlement of his liability under the guaranty.

Taxpayer thereupon made a proposition to the Bank that he would pay off his obligation under the guaranty provided the Bank would extend to him certain accommodations and would take his note for $250,000 properly secured, in full settlement. The Bank considered the taxpayer's proposition and finally accepted it and agreed to take his note for $250,000 in full settlement of his prior obligation under the guaranty, represented by his own note for $125,000 and his endorsement on C. W. Gold's note in the same amount.

37 Accordingly, taxpayer executed his note for $250,000 and delivered it to the Bank, and the Bank delivered to him the two notes marked paid and relieved him of all further liability under the guaranty. Both the taxpayer and the Bank understood that this was to be a final settlement and payment of his prior obligation under the guaranty, and the transaction was so treated on the books of the Bank, as well as on taxpayer's records.

C. W. Gold died insolvent in 1932, but the condition of his estate was not definitely known until his executor's report was made in 1933, and taxpayer continued to look for reimbursement from Mr. Gold's estate until 1933.

Taxpayer, accordingly, in his return for 1932, claimed a deduction of $125,000 on account of the loss arising under his guaranty to the Bank. No loss was claimed in 1932 as to C. W. Gold's part of the guaranty because the taxpayer's claim for contribution and reimbursement from C. W. Gold's estate was still outstanding.

In 1933 it was definitely ascertained that C. W. Gold's estate was wholly insolvent and that taxpayer's claim for contribution was worthless. Taxpayer, accordingly, claimed a deduction in his return for 1933 of $125,000 on account of C. W. Gold's note

which he held, and that loss was allowed by the Commissioner as a proper deduction for 1933.

Subsequently, however, the Commissioner disallowed the loss of $125,000 claimed by petitioner in his return for 1932, upon the theory that the entire loss occurred in 1931, notwithstanding the fact that the Commissioner had also allowed the loss on the C. W. Gold note for 1933.

38 The North Carolina Bank & Trust Co. went into receivership in 1933, and in November 1933 taxpayer's note for $250,000 was sold by the Bank's Receiver to Ethel Clay Price and Kathleen Price Bryan, wife and daughter of taxpayer, in exchange for $250,000 in bonds of North Carolina B. & T. Buildings, Inc., a subsidiary of the North Carolina Bank & Trust Co. Taxpayer's note is now held by Mr. Bryan as trustee for Mrs. Price and Mrs. Bryan.

In the proceeding before the Board the taxpayer contended that his loss under his guaranty of the assets of Atlantic Bank & Trust Co. became definite and fixed in March 1932, when he was called upon by the Bank for the first time for payment of his liability thereunder: that taxpayer made a proposition to the Bank to pay off his obligation under the guaranty by giving to the Bank his own secured note for $250,000 under certain terms and conditions: that his proposition was accepted by the Bank and his liability under the guaranty finally settled and paid in full and all further obligation wiped out, and it was so treated and considered both by the Bank and by the taxpayer—that taxpayer's loss thereby became fixed and determined and his estate reduced accordingly by that amount, and hence that the loss was sustained at that time.

The Commissioner contended first that the loss occurred in 1931, because the Class B assets had so declined in value that the Bank called upon taxpayer and the other guarantors to execute their notes for $125,000 each in June 1931, and therefore the loss was fixed at that time. On the other hand, the Commissioner contended next that the loss has not yet occurred because the taxpayer merely renewed or substituted a new note of

39 $250,000 in lieu of two prior notes for $125,000 each, and hence, under the rule in Eckert v. Burnet, 280 U. S. 140, the loss will not occur until the taxpayer pays the latter note.

The Board found as facts that the Class B assets became worthless in 1932: that the taxpayer's liability under the guaranty became fixed and determined when that fact became known and the Bank called upon taxpayer for payment under his guaranty in March 1932; and that the two notes for $125,000 each which were executed pursuant to the guaranty, were paid when tax-

payer's offer was accepted by the Bank and his secured note for $250,000 was taken by the Bank and the two prior notes delivered to taxpayer in March 1932. Nevertheless and notwithstanding these findings of fact as to the payment and discharge of the prior obligation, the Board held that taxpayer could not deduct the loss in 1932 because taxpayer did not part with cash at that time. Citing Eckert v. Burnet, 283 U. S. 140, as its authority.

IV

Taxpayer states that in the record and proceeding before the Board of Tax Appeals and in the decision and final order of its determination entered by the Board, manifest error occurred and intervened to the prejudice of the taxpayer, and the taxpayer accordingly assigns the following errors which he avers occurred in said record, proceeding, decision, and final order entered by the Board, to wit:

1. The Board erred in failing to decide the case upon the basis of its own findings of fact.

2. The Board erred in holding that the payment of taxpayer's obligation under the guaranty did not result in a deductible loss in 1932, within the meaning of the revenue acts.

3. The Board erred in holding that the payment of the two notes representing taxpayer's obligation under the guaranty did not result in a deductible loss in 1932, within the meaning of the revenue acts.

4. The Board erred in holding that the acceptance by the Bank of taxpayer's offer of settlement of his liability under the guaranty, and the execution and delivery of taxpayer's secured note for $250,000, pursuant to said settlement, did not result in a deductible loss to the taxpayer in 1932.

5. The Board erred in holding that the transaction between the taxpayer and the Bank, which the Board has found as a fact, constituted payment and discharge of the taxpayer's obligation under the guaranty, did not result in a deductible loss in 1932.

6. The Board erred in holding that the payment of an obligation by a taxpayer does not result in a loss unless the payment is made in cash.

7. The Board erred in holding that no loss was deductible under the circumstances, notwithstanding the fact that the Bank agreed to accept taxpayer's secured note as payment and discharge of his prior obligation to the Bank, and both parties treated the transaction as payment in their accounts and records.

8. The Board erred in holding that even though the transaction constituted payment and discharge of petitioner's prior obligation under well-established principles of general law, neverthe-

less it did not result in a deductible loss, because taxpayer did not part with cash.

41 9. The Board erred in holding in effect that a taxpayer can not use money borrowed from a bank on his own secured note, to pay and discharge his liability as guarantor under an entirely different obligation to that bank.

10. The Board erred in deciding the case upon the authority of Eckert v. Burnet, supra.

11. The Board erred in failing to hold that the payment and discharge of taxpayer's contingent liability under the guaranty through the acceptance, by the Bank, of a new and entirely different obligation, did not result in a deductible loss in 1932.

12. The Board erred in failing to decide the case for the taxpayer upon the facts of record.

Wherefore, the taxpayer petitions that the decision and final order of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Fourth Circuit; that a transcript of the record be transmitted to the Clerk of said Court for filing, and that appropriate action be taken to the end that the errors complained of may be reviewed and corrected by the said Court.

(S) C. R. WHARTON.
C. R. Wharton,
(S) D. H. BLAIR.
D. H. Blair,
(S) G. D. BRABSON.
G. D. Brabson,

404 Transportation Building, Washington, D. C.,
Counsel for petitioner.

42 [*Duly sworn to by Julian Price; jurat omitted in printing.*]

43 In United States Circuit Court of Appeals for the Fourth Circuit

[Title omitted.]

Notice of filing petition for review

Filed Feb. 6, 1939

To Honorable GUY T. HELVERING,
Commissioner of Internal Revenue, Washington, D. C.

SIR: You are hereby notified that the above-named petitioner did, on the 6th day of February 1939, file with the Clerk of the United States Board of Tax Appeals of Washington, D. C., a

Petition for Review by the United States Circuit Court of Appeals for the Fourth Circuit, of the Decision of the Board heretofore rendered in the above-entitled case. A copy of the Petition for Review and the assignments of error as filed, is hereto attached and served upon you.

C. R. WHARTON.
C. R. Wharton.
D. H. BLAIR.
D. H. Blair.
GEO. D. BRABSON.
George D. Brabson.
404 Transportation Building, Washington, D. C.
Counsel for Petitioner on Review.

Personal service of the above and foregoing notice, together with copy of the Petition for Review and assignments of error mentioned therein, is hereby acknowledged this 6th day of February 1939.

(S) J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

44 In United States Circuit Court of Appeals for the Fourth Circuit

[Title omitted.]
[File endorsement omitted.]

Designation of points to be urged

Filed April 7, 1939

To Honorable GUY T. HELVERING,
Commissioner of Internal Revenue, Washington, D. C.

You are hereby notified that the petitioner on review hereby designates the following points which are to be urged upon appeal of this case;

1. The Board erred in failing to decide the case upon the basis of its own findings of fact.

2. The Board erred in holding that the payment of taxpayer's obligation under the guaranty did not result in a deductible loss in 1932, within the meaning of the revenue acts.

3. The Board erred in holding that the payment of the two notes representing taxpayer's obligation under the guaranty did not result in a deductible loss in 1932, within the meaning of the revenue acts.

4. The Board erred in holding that the acceptance by the Bank of taxpayer's offer of settlement of his liability under the guaranty, and the execution and delivery of taxpayer's secured
45 note for $250,000, pursuant to said settlement, did not result in a deductible loss to the taxpayer in 1932.

5. The Board erred in holding that the transaction between the taxpayer and the Bank, which the Board has found as a fact, constituted payment and discharge of the taxpayer's obligation under the guaranty, did not result in a deductible loss in 1932.

6. The Board erred in holding that the payment of an obligation by a taxpayer does not result in a loss unless the payment is made in cash.

7. The Board erred in holding that no loss was deductible under the circumstances, notwithstanding the fact that the Bank agreed to accept taxpayer's secured note as payment and discharge of his prior obligation to the Bank, and both parties treated the transaction as payment in their accounts and records.

8. The Board erred in holding that even though the transaction constituted payment and discharge of petitioner's prior obligation under well-established principles of general law, nevertheless it did not result in a deductible loss, because taxpayer did not part with cash.

9. The Board erred in holding in effect that a taxpayer cannot use money borrowed from a bank on his own secured note, to pay and discharge his liability as guarantor under an entirely different obligation to that bank.

10. The Board erred in deciding the case upon the authority of Eckert v. Burnet, 280 U. S. 140.

11. The Board erred in failing to hold that the payment and discharge of taxpayer's contingent liability under the
46 guaranty through the acceptance, by the Bank, of a new and entirely different obligation, did not result in a deductible loss in 1932.

12. The Board erred in failing to decide the case for the taxpayer upon the facts of record.

Respectfully,

GEO. D. BRABSON,
Counsel.

Service of a copy of the above Desiguation is hereby acknowledged this 7th day of April 1939.

J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

47 In United States Circuit Court of Appeals for the Fourth Circuit

[Title omitted.]

Praecipe for record

Filed April 6, 1939

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit, and deliver to the Clerk of the United States Circuit Court of Appeals for the Fourth Circuit, two copies duly certified as correct of the following documents and records in the above-entitled cause, in connection with the Petition for Review by the said Circuit Court of Appeals for the Fourth Circuit, heretofore filed by the above-named petitioner:

1. Documentary entries of all proceedings before the Board.

2. Pleadings before the Board, including: (a) Petition and annexed copy of deficiency notice; (b) Answer.

3. Opinion and decision of the Board.

4. Petitioner's motion for reconsideration by the entire Board, and order of the Board denying the motion. (Not of record.)

48 5. Petition for Review, together with proof of service of notice of filing Petition for Review and of service of a copy of the Petition for Review.

6. Orders, if any, enlarging the time for preparation of the record and transmission and delivery of the record not included in record.

7. This praecipe.

8. Designation of points to be urged.

(Sgd.) GEORGE D. BRABSON.
George D. Brabson.
Transportation Building, Washington, D. C.,
Attorney for Petitioner on Review.

Service of a copy of the within praecipe is hereby admitted this 6th day of April 1939. Agreed to.

(Sgd.) J. P. WENCHEL,
Attorney for Respondent on Review.

49 [Clerk's certificate to foregoing transcript omitted in printing.]

50 **In United States Circuit Court of Appeals for the Fourth Circuit**

No. 4480

JULIAN PRICE, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

On Petition to Review the Decision of the United States Board of Tax Appeals

April 24, 1939, the transcript of record is filed and the cause docketed.

Certified copy of order enlarging time to file record

Filed April 24, 1939

For cause appearing of record, it is ordered: That the time for transmission and delivery of the record sur petition for review of the above entitled proceeding by the United States Circuit Court of Appeals, Fourth Circuit, be, and it is hereby, extended to May 1, 1939.

(S) C. R. ARUNDELL,
Member.

Dated: Wash., D. C., April 7, 1939.

Now, April 22, 1939, the foregoing is certified from the record as a true copy.

[SEAL]

B. D. GAMBLE,
B. D. Gamble, *Clerk,*
U. S. Board of Tax Appeals.

51 April 26, 1939, the appearance of Julius C. Smith and C. R. Wharton is entered for the petitioner.

Same day, the appearance of James W. Morris, Assistant Attorney General, and Sewall Key, Special Assistant to the Attorney General, is entered for the respondent.

April 27, 1939, the appearance of D. H. Blair and Geo. D. Brabson is entered for the petitioner.

May 23, 1939, brief and appendix on behalf of the petitioner filed.

June 8, 1939, the appearance of Berryman Green, Special Assistant to the Attorney General, is entered for the respondent.

Same day, brief on behalf of respondent filed.

June 26, 1939, reply brief on behalf of petitioner filed.

In United States Circuit Court of Appeals

Minute entry of argument and submission

June 29, 1939 (June term, 1939), cause came on to be heard before Parker and Northcott, Circuit Judges, and H. H. Watkins, District Judge, and is argued by counsel and submitted.

July 21, 1939, motion to withdraw appearance of James W. Morris, Assistant Attorney General, is filed.

In United States Circuit Court of Appeals

Order granting motion to withdraw appearance of James W. Morris, Assistant Attorney General

Filed July 24, 1939

On motion of the respondent in the above entitled
52 cases to withdraw the appearance of James W. Morris, as counsel for said Respondent, in view of the fact that Mr. Morris has resigned as Assistant Attorney General, and is now an Associate Justice of the United States District Court for the District of Columbia,

It is ordered by this Court that said motion be, and the same is hereby, granted, and that the appearance of James W. Morris be withdrawn as counsel for the Respondent in the above entitled cases.

July 22, 1939. JOHN J. PARKER,
Senior Circuit Judge.

53 In United States Circuit Court of Appeals,
Fourth Circuit

No. 4480

JULIAN PRICE, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

On Petition to Review the Decision of the United States Board of Tax Appeals

(Argued June 29, 1939. Decided August 28, 1939)

Before PARKER and NORTHCOTT, Circuit Judges, and H. H. WATKINS, District Judge

George D. Brabson and Julius C. Smith (C. R. Wharton, and D. H. Blair on brief) for Petitioner, and Berryman Green, Spe-

cial Assistant to the Attorney General (Sewall Key, Special Assistant to the Attorney General, on brief), for Respondent.

Opinion

Filed August 28, 1939

PARKER, Circuit Judge:

This is a petition to review a decision of the Board of Tax Appeals, approving a deficiency assessment for the year
54 1932. The question involved relates to the deductibility of a loss which taxpayer claims to have sustained in that year on a contract of guaranty previously executed. The Board denied the deduction on the ground that taxpayer, who made his return on the cash receipts and disbursements basis, gave a note covering the loss and that this note was not paid until the year following.

The taxpayer, Julian Price, is president of the Jefferson Standard Life Insurance Company, which in the year 1929 was a large stockholder in the Atlantic Bank and Trust Company of Greensboro, N. C. In September 1929 the last-named institution was merged with the North Carolina Bank and Trust Company; and pursuant to the plan of merger certain assets of the Atlantic Bank, called "A" assets, were accepted conditionally by the North Carolina Bank, and certain other assets, called "B" assets, were pledged to that bank with authority to charge against them any losses which might be established in the "A" assets. At the same time, taxpayer and three other stockholders of the Atlantic Bank executed a guaranty agreement to the effect that, if the North Carolina Bank failed to realize a certain sum from the "A" assets within two years, they would make up the deficiency so ascertained in an amount not exceeding $500,000.00. The period for realizing on the "A" assets under the terms of the guaranty was subsequently extended for an additional year, or until sometime within the year 1932.

In June 1931 the president of the North Carolina Bank advised the four guarantors that the "B" assets were not in such shape that the bank could use them to the extent necessary for banking purposes, and requested them to put their guaranty into bankable form so that it could be used by the bank to obtain credit. Whereupon taxpayer executed and delivered to the bank his note for $125,000.00 and indorsed the note of C. W. Gold, another one of the guarantors, for a like amount. He also borrowed from his wife certain stocks which he deposited as collateral security to the notes. At this time, the "B" assets
55 were still pledged as security for realization on the "A"

assets; and in August 1931 they were valued upon an appraisal at $529,947.44, or an amount in excess of the guaranty made by taxpayer and his fellow guarantors. The Board finds that: "At the end of 1931, the guaranty agreement was still in force and effect. The 'B' assets were still in the hands of the North Carolina Bank, as trustee, and were still in the process of collection. No demand had ever been made upon petitioner for the payment of any part of his obligation under the guaranty. While it was known that there would be some loss to the guarantors, it was not definitely known throughout 1931 what the amount of the loss would be, and the guarantors had every reason to believe there would be a substantial reimbursement from the 'B' assets of any losses."

Financial conditions in Greensboro took a turn for the worse in the early part of 1932, collections on the "A" and "B" assets declined, and it was soon apparent that there was no possibility of recovering anything further from the "B" assets. Consequently the North Carolina Bank decided to make collection on the guaranty as to the "A" assets, and called the guarantors to make good their guaranty. Taxpayer, thereupon, executed his note for $250,000.00 to the bank in settlement of his liability and that of Mr. Gold, upon whose note he was indorser; and the finding of the Board with respect to this crucial matter is as follows:

"In the latter part of March 1932, petitioner, in his discussions with officials of the North Carolina bank, was informed that the bank had decided that the possibilities of collecting anything on the 'B' assets were remote and that there was no hope of any relief from these assets. The bank requested that petitioner make a final settlement of his obligation under the two notes and the guaranty to the bank. Petitioner proposed to pay the two notes (his own note and Gold's note on which he was endorser) by giving the bank his note for $250,000. The
56 bank accepted, and the C. W. Gold note in the amount of $125,000, endorsed by petitioner, and petitioner's individual note in the same amount were paid by the note of petitioner in the amount of $250,000, dated March 28, 1932. Upon the delivery of this note for $250,000 the bank marked 'paid' and turned over to petitioner the two notes which had been executed under the guaranty agreement. Both petitioner and the bank considered this to be a final payment of the two notes given under the guaranty."

Taxpayer at first deposited as collateral with the $250,000 note the stocks which he had borrowed from his wife and deposited as collateral to the accommodation notes given by himself and Gold in the preceding year. In the following December, how-

ever, he substituted securities of his own in lieu of these. In November 1933, the note was transferred by the Conservator of the Bank to taxpayer's wife and daughter and was held by an agent as trustee for them at the time of the hearing before the Board.

Taxpayer deducted only $125,000 as a loss on account of this transaction in 1932, that being his individual loss as guarantor; and the propriety of that deduction is the only matter before us. The $125,000 that he paid on account of his indorsement for C. W. Gold he deducted as a loss in 1933; and that deduction is not here in controversy. As to the propriety of deferring the latter deduction until 1933, it appears that Gold died in 1932 and it was necessary for taxpayer to look to his estate for reimbursement. Not until 1933 did it become apparent that the estate was insolvent and that taxpayer could expect no reimbursement therefrom.

Upon these facts the only question that arises in the case is when did the taxpayer sustain the $125,000 loss on his guaranty. We think it clear that he sustained it in 1932. He did not sustain it in 1931, because at that time it was not definitely ascertained that he would sustain a loss, or, if so, what the loss would be. He did not sustain it when he paid the note; for that was but the payment of a debt incurred when the loss was
57 sustained, and we have recently held that the payment of a debt results in no deductible loss. U. S. v. Little War Creek Coal Co., 4 Cir. 104 F. 2d 483.

How a deductible loss must be evidenced is thus set forth in Regulations 86, Article 23 (e): "In general losses for which an amount may be deducted from gross income must be evidenced by closed and completed transactions, fixed by identifiable events, bona fide and actually sustained during the taxable period for which allowed." And see Rhodes v. Commissioner, 6 Cir. 100 F. 2d 966, 969. The loss sustained by the taxpayer in 1932 falls squarely within the terms of this regulation. The guaranty given the bank and the payment thereunder were closed and completed transactions. The closing was fixed by an identifiable event, viz. the giving of the $250,000 note as the primary obligation of the taxpayer, and not as a mere guaranty or accommodation, and the surrender of the two notes which had been executed under the guaranty agreement. There can be no question as to the loss being "bona fide and actually sustained" within the period. The Board finds that "The bank requested that petitioner make a final settlement of his obligation under the two notes and the guaranty to the bank," and that, when petitioner delivered his note for $250,000 and the bank turned over to him the two notes which had been executed under the guaranty agreement, "Both

petitioner and the bank considered this to be a final payment of the two notes given under the guaranty." Prior to this transaction taxpayer was liable on his guaranty and on the two notes given as accommodation thereunder; but his loss under the guaranty had never been determined and his liability was of a secondary character, for even on the notes executed in 1931 he was liable only as an accommodation maker. In giving the $250,000 note, however, he faced realities and accepted his loss. His liability on the note thus executed was primary and unconditional.

58 The fact that taxpayer instead of meeting his loss with a cash payment gave a note in settlement, does not change the situation as to when the loss occurred; for the giving of the note could not postpone the loss. The loss was accepted and the note given created a bona fide indebtedness of an entirely different character from that which had theretofore existed. It will not do to say that taxpayer sustained the loss when he paid the debt and not when he incurred it for the purpose of meeting the loss: for one does not sustain a loss by merely paying a debt for which he himself is primarily liable, nor is the loss deferred by contracting a debt with which to pay it. The able attorney representing the Commissioner very properly admitted on the argument that, if taxpayer had obtained the $250,000 to meet the loss by giving the note to another bank, he would have been entitled to the deduction claimed; but surely his right to the deduction cannot depend upon the identity of the bank which extends credit to him.

It is argued that the fact that taxpayer is on the cash receipts and disbursements basis instead of the accrual basis makes a difference; but we do not think so. The question is not one of accruing a loss to occur in the future, but of dealing with a loss that has already occurred; and, as heretofore stated, the occurrence of the loss cannot be said to be postponed merely because credit is obtained with which to meet it. This seems very clear if a simple illustration be taken: If A and B, indorsers on the note of an insolvent corporation, are called for payment, and A discharges his half of the liability in cash while B gives his individual note, payable in the following year but amply secured (as was the case here) in discharge of his liability, can it be said that the loss is sustained by A in one year and B in the next? To ask the question is to answer it. Any such rule would not only shock the common sense of practical men, but would also put it within the power of a taxpayer to spread losses of this character over a number of years, by the simple expedient of giving

59 a note or notes in settlement of the loss and claiming deductions as the notes are paid.

There is a difference, of course, between a m[illegible] postponing of a pending loss on a secondary obligation and n[illegible]eting the loss, as the taxpayer did here, with the execution of a primary obligation. In the one case, the loss may never be sustained; in the other, it is sustained when the primary obligation is given. True, a taxpayer on the cash receipts and disbursements basis cannot be said to have sustained a loss until he has parted with money or money's worth; but when he executes a bankable note, secured by collateral, he has parted with money's worth. The value of his estate is decreased by the amount of the note as a result of the transaction.

The facts of the case, in final analysis, amount to a borrowing by taxpayer from the bank of funds with which to meet the liability on his guaranty and the application of the proceeds of the loan to that purpose; and we know of no principle of law or of justice which would deny him the right to deduct the loss arising from his guaranty until the loan is repaid. A case very much in point is Crain v. Commissioner, 8 Cir. 75 F. 2d 962. In that case taxpayer and another became obligated to pay obligations of a corporation in which they were stockholders in the sum of $80,000. In 1916 the other person paid the $80,000 in cash and took taxpayer's note for $40,000, which taxpayer did not pay until 1919. Taxpayer sought to take deduction for his part of the loss in the year 1919 when he paid the note. In holding that he might not do this, the court said:

"But in the year 1916, the amount of loss sustained became definitely certain, and the whole of it was actually paid by Wesson. Since the taxpayer did not himself have on hand enough cash to pay his half, he agreed with Wesson that the latter should advance all of the money in payment of the loss, and the taxpayer would make to Wesson a note for the taxpayer's half of such loss.

60 "In fair effect, what the taxpayer did in 1916 was to borrow $40,000 in money with which to pay the loss, now here in dispute, as to the date of its accrual for taxing purposes. It seems clear, from the facts here and the ruled cases, that the loss occurred in 1916. Avery v. Commissioner, C. C. A., 22 F. 2d 6, 55 A. L. R. 1277; Darling v. Commissioner, C. C. A., 49 F. 2d 111. Did the giving of the note to Wesson have the effect to lawfully postpone deduction of the loss from income till the year in which the note was paid?

* * * * * * *

"If the taxpayer had himself actually paid in cash his part of the loss in 1916 it would hardly be contended that he could not in that year have charged the sum paid as a proper deduction from

his income for that year. It is difficult to see how the situation was changed merely because he was forced to borrow money from another with which to pay his part of the loss."

Another case very much in point is Jenkins v. Smith, 21 F. Supp. 433. In that case a taxpayer had executed a bond to a bank in precarious condition guaranteeing the deposit of collateral which was to become the property of the bank in the event of its insolvency. The bank became insolvent and its affairs were taken over by another bank, which called upon taxpayer to make good his obligation under the bond. He thereupon executed his note to the last-named bank to borrow a sufficient sum to meet the obligation and gave his check in extinguishment thereof. It was held that a deductible loss resulted. The court said:

"The deduction was proper and plaintiffs must prevail if, under all the circumstances, the obligation on the bond was paid. The defendant urges, however, that there was no payment in fact, but only in form, since the decedent remained obligated to the First National Bank & Trust Company for the same amount, evidenced by a new note. He parted with no cash in 1933, but merely borrowed from his payee in order to pay the same payee.

"In my opinion, the obligation on the bond was dis-
61 charged by the acceptance by the First National of the check as payment. Where or how the decedent obtained the money with which to make the check good is immaterial. The acceptance of the check as payment discharged the obligation, even though it created an overdraft. A new cause of action arose upon the check. The First National could no longer have sued the decedent on the bond. The bank knew of the overdraft, but was satisfied to take its chances on the new obligation. The bond transaction was closed.

"The credit to the decedent's account, made on the same day, was the result of a new transaction, initiated by a promissory note to the bank secured by new collateral. It was in no sense an extension of time for payment of the old debt. It was a new contract of a substantially different nature."

Directly in point is the Board's decision in A. W. D. Weis v. Commissioner, 13 B. T. A. 1284. In that case, as here, taxpayer kept his books on the cash receipts and disbursements basis. A partnership in which he was interested failed in the year 1919, and he was called by a bank for the payment of partnership paper upon which he was liable and gave the bank his personal note, which was renewed from time to time and not paid until 1923. The Board said:

"We are of the opinion that all the losses here in question were sustained in the years in which the several investments became worthless. In such respective years each of the deals became a

closed transaction and the petitioner's net assets were reduced in the amount of the loss sustained. It is not material whether such losses were met by the payment of cash from funds in hand or with cash borrowed from the bank and evidenced by notes payable in a subsequent year. The loss had been sustained and the transaction had been closed by a cash payment. The use of the petitioner's credit to secure funds from the bank was a new and different deal and had no more to do with the petitioner's tax liability than any other borrowing that he did in the taxable year."

62 The Weis case deals with another situation which demonstrates the unsoundness of the general proposition that a taxpayer on a tax receipts and disbursements basis cannot be said to sustain a loss so long as he does not meet the loss with a cash payment. In a transaction separate and distinct from the one described, taxpayer had given his note for $37,500 to a corporation for stock issued to him. The corporation went into bankruptcy in 1921 and taxpayer's investment therein became a total loss in that year although he did not pay the note until 1925. It was held that he was entitled to take deduction for the loss in 1921 and not in 1925.

The chief reliance of the Commissioner is the decision of the Supreme Court in Eckert v. Burnet, 283 U. S. 140; but we do not regard that decision as controlling here. In that case the taxpayer and another were indorsers on paper of a defunct corporation. They executed a joint note to the bank, and destroyed the old notes. Taxpayer sought to deduct half of the sum of these notes as a worthless debt. The court said: "The petitioner treats the case as one of an investment that later turns out to be bad. But in fact it was the satisfaction of an existing obligation of the petitioner, having, it may be, the consequence of a momentary transfer of the old notes to the petitioner in order that they might be destroyed. It is very plain, we think, that the words of the statute cannot be taken to include a case of that kind." The court went on to say further: "As happily stated by the Board of Tax Appeals, the petitioner 'merely exchanged his note under which he was primarily liable for the corporation's notes under which he was secondarily liable, without any outlay of cash or property having a cash value.' A deduction may be permissible in the taxable year in which the petitioner pays cash. The petitioner says that it was definitely ascertained in 1925 that the petitioner would sustain the losses in question. So it was, if the petitioner ultimately pays his note. So was the tax
63 considered in United States v. Mitchell, 271 U. S. 9, 12, but it could not be deducted until it was paid."

We consider this case as definite authority only for the holding that a loss of the character set forth is not deductible under the "bad debt" provision of the statute (Burns Mfg. Co. v. Commissioner, 9 Cir. 59 F. 2d 504, 507), although the language does indeed go further and lay down the proposition that where there is a mere deferring of a loss by the renewing of an obligation, the loss may not be deducted until the obligation is paid, a proposition which we are not disposed to question. That it was not intended to prevent by that decision the taking of a loss in a case such as this, where the loss is evidenced by a closed transaction, but merely to prevent the taking of a supposed loss which has never been realized, is indicated by the decision in Burnet v. Logan, 283 U. S. 404, 413, where the court refers to the Eckert decision as follows: "Ordinarily, at least, a taxpayer may not deduct from gross receipts a supposed loss which in fact is represented by his outstanding note. Eckert v. Commissioner of Internal Revenue, ante, p. 140. And, conversely, a promise to pay indeterminate sums of money is not necessarily taxable income. 'Generally speaking, the income tax law is concerned only with realized losses, as with realized gains.'" In other words, the taxpayer may not take deduction for a loss where what he has done is merely to postpone the evil day of reckoning. He may take the deduction where he has met the evil day and the loss has been realized. The fact that he borrows money to meet it is immaterial; the fact that he borrows to meet an outstanding obligation out of which the loss arises is immaterial; and the fact that he borrows from the person to whom the obligation is due is immaterial, provided that there is, as there was here, a real payment of such obligation in money or money's worth and not a mere extension or renewal.

The Commissioner relies also upon Jenkins v. Bitgood, 2 Cir. 101 F. 2d 17, and Hart v. Commissioner, 1 Cir. 54 F. 64 2d 848. The former relates to the deductibility of losses in stock for which a note was given in payment. It has no applicability to the case at bar except insofar as certain reasoning of the opinion may be persuasive. In this connection, however, we will say that we are not impressed with the reasoning that a taxpayer may not deduct in the year in which it occurs a loss sustained as the result of a purchase of stock, merely because he has given his note for the purchase of the stock payable in a succeeding year. The Hart case deals with the deductibility of interest, where the interest is not in fact paid but a note is given for it. This, of course, is a mere deferring of payment and not at all the sort of thing involved in the transaction before us.

The whole question in the case at bar comes to this: Was there a mere postponement of the loss by the renewal of the existing

obligation? Or was there a realization of the loss by the discharge of the existing obligation and the assumption by taxpayer of an independent obligation of a different character? We think that the latter is the case. The loss arising out of the guaranty given the bank was liquidated and discharged by the taxpayer. He discharged that liability, not with money, but with money's worth, i. e., with his bankable note amply secured by collateral. The case is no different from what it would have been had he borrowed money from another bank on this note and used the proceeds for the purpose for which he used the note itself. The old obligation was not carried forward nor was the taking of the loss postponed. The loss was actually sustained when the liability on the guaranty was met and discharged; and it cannot affect taxpayer's right to deduction on account thereof that he met it by what was in effect a borrowing of money.

For the reasons stated, the decision of the Board will be reversed.

Reversed.

65 In United States Circuit Court of Appeals, Fourth Circuit

No. 4480

JULIAN PRICE, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

On petition to Review the Decision of the United States Board of Tax Appeals.

Judgment

Filed and Entered August 28, 1939

This cause came on to be heard on the transcript of the record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the decision of the said Board of Tax Appeals, in this cause, be, and the same is hereby, reversed; and that this cause be, and the same is hereby, remanded to the United States Board of Tax Appeals for further proceedings in accordance with the opinion of the Court filed herein.

JOHN J. PARKER,
Senior Circuit Judge.

AUGUST 28, 1939.

Recital as to issuance of mandate.

On another day, to wit, September 28, 1939, the mandate of this Court, in this cause, is issued and transmitted to the
66 United States Board of Tax Appeals, at Washington, D. C., in due form.

[Clerk's certificate to foregoing transcript omitted in printing.]

U. S. GOVERNMENT PRINTING OFFICE 1939

Supreme Court of the United States

Order allowing certiorari

Filed January 15, 1940

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Fourth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

U. S. GOVERNMENT PRINTING OFFICE 16—